

OFFICE OF THE DIRECTOR

Date: 17 August 1977

TO: The Director

20 AUG 1977

FROM:

[REDACTED]

77-5205/B

SUBJECT: Treasury View on Taxing Overseas Allowances

REMARKS:

[REDACTED] our man at Treasury, reported today that your letter opposing taxation on overseas allowances which you sent to the Secretary of the Treasury following his raising the subject at a Cabinet meeting, was one of the best received. It, along with others, helped to convince the Secretary not to support such taxation proposals.

While the decision is up to the Congress, [REDACTED] thought you'd appreciate knowing the Secretary's decision and that your letter was a factor in it.

DDO_____

1 August 1977

The Honorable Michael Blumenthal
The Secretary of the Treasury
Washington, D.C. 20220

Dear Mike,

At the Cabinet Meeting on 25 July 1977, you mentioned the possibility of legislation which would rescind Section 912 of the Internal Revenue Code, thereby making allowances paid to overseas personnel taxable income to them. I appreciate your raising the subject at this level and would like to take this opportunity to comment from the CIA viewpoint.

During the past two years, there has been significant concern in the Agency on the part of management, as well as the employees, with respect to this legislation. It would have very serious implications for all agencies with personnel overseas, since it would mean that employees assigned abroad would thereafter be faced with the payment of substantially increased income taxes.

There are a number of reasons why we feel that a revision of the law would be a mistake, and we are prepared to document these in as much detail as necessary. Basically, however, they fall into three categories:

First, the burden of the change would be borne by employees, particularly those in the lower grades, and it would then not be possible to persuade employees to accept the overseas obligations. Further, the short-term impact on complements abroad could be devastating, both to morale and to willingness of employees to stay abroad.

Second, there seems to be an assumption that, if Section 912 is rescinded, the other committees of Congress will increase the allowances to help offset some of the taxes the employees will pay.

In discussions with some of the committees, however, they have indicated that they do not believe that the Congress would increase appropriations for this purpose.

And, finally, the requirement to report all of these expenditures in the separate pay accounts of the thousands of employees, and otherwise facilitating enforcement of the new law by the Internal Revenue Service, would result in an enormously increased administrative workload. We believe, in fact, that the additional appropriations and increased workload would nullify any benefit the Government might otherwise realize as a result of increased revenue from the employee/taxpayers.

The CIA is represented on the Interagency Committee on Overseas Allowances and Benefits, which is still in liaison with the working level in the Treasury Department to assure that all of the related facts are available to your staff. I sincerely urge that these facts be given careful consideration, because our overseas operations will be vitally affected if key employees conclude that their financial best interests require that they avoid service abroad.

Yours,



STANSFIELD TURNER

AUG 23 12 33 PM '77

ER

STAT SSA/DDA/ [] 1m (26 July 1977)

Distribution:

Orig - Addressee

1 - DCI

1 - ADDCI

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Executive Registry

Approved For Release 2004/03/11 : CIA-RDP80M00165A002100010004-7
MEMORANDUM FOR: Mr. Baker

Doubt this needs DCI approval --- why not
tell Mike to prepare notification and you
will release. DCI's policy position is in
hand via his 1 August letter.


B. C. Evans

4 August 1977
(DATE)

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STAT

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OUTGOING
TELEGRAM

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PAGE 01 STATE 180195
ORIGIN A-01

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INFO OCT-01 OPR-02 MMO-04 SS-15 AF-10 ARA-14 EA-09
EUR-12 NEA-10 IO-14 ISO-00 /092 R

DRAFTED BY A: JMTTHOMAS;
APPROVED BY A: JMTTHOMAS
A/O: LJDUPRE
A/ALS: NLIZOTTE (BY PHONE)
M/MO: JCLARK (IN DRAFT)
M-DESIGNATE: BREAD

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FM SECSTATE WASHDC
TO ALL DIPLOMATIC AND CONSULAR POSTS PRIORITY

UNCLAS STATE 180195

INFORM CONSULS

E. O. 11652: N/A

TAGS: ALOW

SUBJECT: RECOMMENDATION ON TAXATION OF ALLOWANCES

REF: STATE A-2879; A-2633; A-1593

1. ON JULY 30 SECRETARY VANCE SPOKE TO SECRETARY OF TREASURY BLUMENTHAL AND SENT HIM A LETTER AND STAFF MEMORANDUM EXPRESSING STRONG OPPOSITION TO PROPOSAL OF TREASURY OFFICE OF TAX POLICY CONSIDERATION OF REPEAL OF SECTION 912 OF THE INTERNAL REVENUE CODE. HE URGED THAT THE PROPOSAL NOT BE SENT FORWARD AS PART OF ANY TAX REFORM PACKAGE AND STATED HIS WILLINGNESS TO TAKE UP THE MATTER WITH HIGHEST LEVELS IF IT SHOULD BE NECESSARY TO DO SO.

2. SECSTATE EXPRESSED HIS JUDGMENT THAT THE PROPOSED REPEAL OF SECTION 912 EXEMPTING THESE OVERSEAS ALLOWANCES FROM TAXATION WOULD HAVE SERIOUS ADVERSE IMPLICATIONS NOT ONLY FOR DEPT OF STATE, BUT FOR ALL OTHER GOVERNMENT AGENCIES WITH CIVILIAN EMPLOYEES SERVING ABROAD. HE NOTED SEVERE TAX IMPACT OF PROPOSAL ON STAFF AS WELL AS OFFICER LEVEL PERSONNEL. HE ALSO STATED THAT OUR EMPLOYEES MUST NOT BE DISADVANTAGED THROUGH TAXATION OF ALLOWANCES WHICH REPRESENT REIMBURSEMENT TO THEM FOR THE UNUSUAL COSTS ASSOCIATED WITH THEIR OVERSEAS ASSIGNMENTS. SUCH

ALLOWANCES SHOULD NOT BE CONSIDERED INCREMENTAL INCOME TO EMPLOYEES.

3. THE SECRETARY REGARDS THIS AS AN EXTREMELY IMPORTANT ISSUE AND BE ASSURED THAT EVERY EFFORT WILL BE MADE TO KEEP ALL EMPLOYEES INFORMED OF ANY DEVELOPMENTS. CHRISTOPHER

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UNCLASSIFIED

THE SECRETARY OF STATE
WASHINGTON

7720070

July 30, 1977

COPIES TO:

M

S/S-S

S/S-S-LF

A

M/MO

RF (jhw)

Dear Mike:

At the Cabinet meeting on July 25, you mentioned that Treasury was considering the taxation of allowances and benefits paid to USG civilian employees overseas as part of the Administration's Tax Reform proposals.

This is of great concern to me. The proposed repeal of Section 912 exempting these overseas allowances from taxation would have most serious adverse implications not only for the Department of State, but for all other government agencies with civilian employees serving abroad. If we are to retain the flexibility we need in the personnel administration of our overseas operations, we must insure that our personnel are not financially disadvantaged through the taxation of allowances which represent reimbursement to them for the unusual costs associated with their overseas assignments. Such allowances should not be considered incremental income to employees. I subscribe fully to the reasons in opposition to the proposal set forth in the attached memorandum.

I urge you not to go forward with the proposed repeal of the overseas allowances exemption. I regard this issue as so important that I would want to take it up with the President if it should be necessary or if you should wish me to do so.

Sincerely,

MICROFILMED
BY S/SI

The Honorable

W. Michael Blumenthal,

Secretary of the Treasury.

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Drafted by: A/ALS:RWeiss:mak

Clearances:

A/ALS:RWeiss

It has been suggested that it is necessary to tax the allowances of government civilians overseas because we want to treat them in the same manner as employees of private industry overseas. The repeal of Section 912 will not contribute toward equal treatment, when the conditions under which each group serves are different in so many ways. Nor should it be suggested that taxation of military allowances and benefits would constitute equal treatment for civilian and military personnel. It must be recognized that different groups with different reasons for being overseas and differing needs and responsibilities are involved. That fact alone argues for the need for separate treatment and procedures to meet the specific needs of each group.

The Overseas Differential Act of 1960 (P.L. 86-707) which authorizes most of the overseas allowances in question, and the House and Senate Reports on the Act, clearly show Congressional recognition that service abroad entails expenses to employees above those which the employees would incur were they stationed in the United States. There has never been any intention to provide overseas employees with monetary advantages over their colleagues who serve at home, except to assure equal treatment, as in the case of cost of living payments. Many misconceptions exist, both in and out of government, as to the true nature of overseas allowances and benefits. If unbalanced treatment truly does exist between employees serving in the U.S. and abroad, methods of correction short of repealing Section 912 must be found.

The Inter-Agency Committee on Overseas Allowances and Benefits has reviewed the existing structure of federal civilian overseas allowances and benefits to arrive at recommendations on a comprehensive allowance program which would, effectively and equitably, meet current requirements for overseas operations. Secretary Vance sent Secretary Blumenthal a copy of the report on July 11 emphasizing the former's agreement with the conclusions of Chapter 4 - Taxation of Allowances.

Since the treatment of allowances for tax purposes is an essential element of the entire allowance structure, all committee members were asked to comment

- 2 -

on the proposed repeal of Section 912 of the Internal Revenue Code. There was agreement by 19 of 20 agencies (Department of Treasury abstained on Chapter 4) that a flat repeal of Section 912 at this time would be grossly inequitable, prejudicial to the operations of the foreign affairs agencies, and without significant benefits to overall U.S. Government operations.

A brief review of some of the more significant overseas allowances will show why it would be inappropriate to subject them to taxation. The essential feature of each of these allowances is that it is intended to defray necessary additional expenses incurred because of overseas service. With the exception of the hardship differential paid to employees at unhealthy, dangerous or otherwise less desirable posts, which is currently subject to taxation, none of the allowances are classified as "premium" allowances.

- The cost-of-living allowance is simply an equalizer designed to offset the difference between the cost of living at an expensive foreign post of assignment and in Washington, D. C. It is not realistic to expect employees to pay additional taxes because prices are higher in some parts of the-world. For example, the cost of living for U.S. Government civilian employees in Geneva is 50% higher than Washington; in Kuwait 35% higher; in Yaounde 30% higher; and in Caracas 15% higher.
- An education allowance is authorized so that all parents employed by the Government overseas can provide their children with the level of education which is available to all children free in the United States. Clearly this is not incremental income and not properly taxable.
- The quarters allowance is also an offset against extraordinary housing expenses

which an employee encounters as a direct result of his assignment in a foreign country. The annual cost of rent and utilities for a typical GS-13 employee is \$7,480 in Rome, \$11,330 in Paris, \$4,730 in Mannheim, \$16,720 in Bahrain, and \$15,350 in Abidjan. With shortages of adequate housing and spiraling rent and utility costs at most foreign locations, the quarters allowance continues to be necessary to assign the right person to the right post at the right time.

If one were to follow the tax methodology of 15% suggested by Assistant Secretary Woodworth of the Office of Tax Policy to the representatives of State, Agriculture, DOD and CIA who met with him, the increase in taxes for a typical GS-13 employee serving abroad would be 54% in Rome, 102% in Paris, 34% in Mannheim, 103% in Bahrain, and 156% in Abidjan, with no increase in disposable income with which to pay it.

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ROUTING AND RECORD SHEET

SUBJECT: (Optional)

Letter to Secretary of Treasury Blumenthal

EX 77-5205

FROM: Michael J. Malanick
Acting Deputy Director for Administration

EXTENSION

NO. DDA 77- 4246

DATE 26 July 1977

TO: (Officer designation, room number, and building)

DATE

RECEIVED

FORWARDED

OFFICER'S INITIALS

COMMENTS (Number each comment to show from whom to whom. Draw a line across column after each comment.)

1. ADDCI

20 JUL 1977

2. *BERNE: SELF-EXPLANATORY*

3. DCI

Rec'd 27 July - 1 AUG 1977

For your information, the Interagency Committee for Overseas Allowances and Benefits will be meeting this Thursday (28 July) with Treasury Department officials at the staff level and once again try to persuade them in our direction.

This paper has been coordinated with the Office of Legislative Counsel.

CENTRAL INTELLIGENCE AGENCY

OFFICE OF THE DEPUTY DIRECTOR

"To DCI

"You requested this type letter at the Monday, 25 July, staff meeting.

/s/Jack Blake"

10 DCI

You requested this type letter at the Monday, 25 July, staff meeting

STAT

26 JUL 1977

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Approved For Release 2004/03/11 : CIA-RDP80M00166A002100010004-7

SUBJECT: (Optional)

77-5205/A

FROM:

Michael J. Malanick
Acting Deputy Director for Administration

EXTENSION

NO.

DDA 77-4419

DATE

3 August 1977

TO: (Officer designation, room number, and building)

DATE

RECEIVED

FORWARDED

OFFICER'S
INITIALS

COMMENTS (Number each comment to show from whom to whom. Draw a line across columns after each comment.)

1. ADDCI

4 AUG 1977

Attached for your information are (a) a copy of a book cable from the State Department to all their posts which explains what the Department is doing vis-a-vis the tax reform package; and, (b) a copy of the final version of the Secretary of State's letter to the Secretary of Treasury. Please note the final paragraph of his letter, which states, "I regard this issue as so important that I would want to take it up with the President if it should be necessary...."

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Subject to your approval, and with the concurrence of the DDO, I would like to send out notification to all our field stations of the existence of State's book cable and the Vance letter and, further, quote the Director's letter to Secretary of Treasury. In addition, you, Admiral Turner, may wish to refer to the position you and the Secretary of State have taken on this matter in your next "Notes" from the Director."

STAT

Michael J. Malanick
Acting Deputy Director for
Administration

Attachments

4 AUG 1977

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EXECUTIVE SECRETARIAT

Routing Slip

TO:		ACTION	INFO	DATE	INITIAL
1	DCI				
2	DDCI		✓		
3	D/DCI/IC				
4	DDS&T				
5	DDI				
6	DDA		✓		
7	DDO		✓		
8	D/DCI/NI				
9	GC				
10	LC		✓		
11	IG				
12	Compt				
13	D/Pers				
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15	DTR				
16	A/DCI/PA				
17	AO/DCI				
18	C/IPS				
19	DCI/SS				
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22					
SUSPENSE		Date			

Remarks:

*DCI's letter prepared
by*

Executive Secretary

STAT